The SaaS Churn Bible

Everything You Need To Know About Identifying & Combating Churn

chargify

Elastic Billing for SaaS

In Partnership With

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Foreword

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Director of Product Marketing at Chargify

Why Churn Matters

Software as a Service (SaaS) was born out of the need to eliminate scalability pains that plagued the traditional software licensing model. Pains such as hardware requirements, manual updates, access limitations, and much more.

While SaaS removed the majority of these pains, it created its own new set of challenges fueled by advancements in cloud computing, diminishing capital requirements, and minimal barriers to entry. The byproduct has resulted in the most competitive landscape the world has ever seen with exponential growth over the past decade that does not show any signs of slowing down.

Companies no longer compete with a handful of vendors—they compete with dozens, and sometimes hundreds of vendors. Switching costs are low. Customer loyalty is diminishing. Industry leaders must be innovative to remain on top while lean, scrappy newcomers threaten them with very attractive alternatives.

True subscription success does not come from deals you close. It comes from the deals you keep by building long-lasting relationships with happy, loyal, engaged customers.

The benefit of the subscription business model—and SaaS—is the ability to grow predictable, recurring revenue. If customers churn just as fast as they convert, your recurring revenue will never be able to reach its true potential.

Karl Stjernstrom

Head of Global Enterprise Partnerships at GoCardless

Churn is the enemy of every SaaS business. A customer who leaves before you have recouped your cost of acquisition is worse than not signing up a customer at all. The fastest growing subscription businesses know this, and are focusing their efforts on developing strategies to combat churn.

Whether you're billing customers by subscription, through invoices or through installment plans, Churn matters. Here at GoCardless, we consider it as one of the Eight Payment Dimensions that drive your business success, alongside Preference, Coverage, Conversion, Cost, Success, Visibility and Cash flow. You can see our consumer report on global payments preferences here.

In this report, we'll take an in-depth look at the different types of Churn that exist, the impact on your SaaS business's bottom line, and the strategies for reducing Churn and increasing customer satisfaction.

A huge thank you to our partners at Chargify for sharing their thoughts on what Churn means to them, which you'll find spread throughout the report.

We hope you find the report useful, and we welcome any feedback you might have at content@gocardless.com.

Introduction

In the simplest form, churn is the result of paying customers becoming non-paying customers, but there is much more to churn than meets the eye. Understanding the different types of churn, ways to quantify it, and actionable steps to reduce it can literally make or break a SaaS company!

There is a statistic that you've probably heard or read dozens of time, but we'll reiterate again because it is an important one—it costs 5x more to obtain a new customer than to keep an existing one.

If that isn't a compelling enough argument, Frederick Reichheld of Bain & Company (the inventor of the net promoter score) uncovered that increasing customer retention rates by 5% leads to a 25% to 95% increase in profit. Not only do loyal customers stick around, they tend to buy more and refer more friends over time.

Churn can either be active (voluntary) or passive (involuntary). While both of these types of churn will result in lost customers, they have very different underlying causes and prevention tactics.

In this eBook, we're going to cover:

- What exactly is the difference between voluntary and involuntary churn
- Different ways to calculate and quantity churn metrics
- Actionable ways to combat both voluntary and involuntary churn—now and overtime
- Real-life tips and tricks from successful, seasoned SaaS leaders

What Is Voluntary Churn?

Voluntary churn is when a customer actively chooses to terminate their service. There are many reasons why this happens but some common ones include:

- What they signed up for did not meet their expectations and/or solve the problems they thought it would solve
- The customer had a bad experience either upfront or throughout the course of their relationship with a company that causes them to look for other alternatives
- There was a misalignment of price and value where the value they received did not justify the money being spent
- Another competing product was brought to their attention and provided a more attractive alternative solution for their needs and/or budget
- The company is going out of business and no longer needs a service (unfortunately, this one is out of your hands)

We will dig deeper into the common causes and solutions, but the important, high-level takeaway is that the right combination of engagement, positive customer experience and perceived value is mission critical to plugging the voluntary churn leak.

What Is Involuntary Churn?

While customer success and product teams work hard to make sure customers continue to get value from their subscriptions, their efforts can be thwarted by losing a customer to preventable payment issues such as expired, cancelled or lost cards. This is involuntary churn!

Every month, SaaS businesses are pointlessly losing 1-4% of their customers. For a business doing 100,000 transactions a month, with an average transaction value of £10, that could mean a loss of £15 million in cumulative revenue over five years. In fact, up to 40% of SaaS customer churn is involuntary.

Patrick Campbell, Co-Founder & CEO, ProfitWell, comments: "20-40% of your churn is actually absolutely needless, stemming from failed, expired, and delinquent credit cards. Let me put that data in perspective for you. If your churn rate is currently 5%, then one to two percentage points of that churn exists for an absolutely needless reason. You're pointlessly losing a lot of money every month."

Involuntary churn (also known as passive churn or delinquent churn) is a particular issue for subscription businesses, who typically capture a customer's payment information at sign up and store for processing future payments, but over time, those details become out of date.

Payment failure rates for SaaS business vary depending on sector and market, but are typically 5-18%. How much of that businesses are able to recover depends on what payment methods you accept and the revenue retention tools/strategy you have in place.

Understanding Churn Calculations

Before we dig into some actionable ways to combat churn, it is important to first understand the different churn calculations so you can have a benchmark of where you are today, identify any red flag metrics, and set smarter goals moving forward...

Subscriber Churn Rate

Subscriber Churn Rate is the rate at which your subscribers are cancelling their subscriptions.

Calculation: Subscriber Churn Count / Start of Period Subscriber Count

Example: If you had 200 subscribers at the start of the period and 10 subscribers churned during that period, the Subscriber Churn Rate would equal 5%.

Close.io CEO, Steli Efti, explains why Subscriber Churn Rate is particularly valuable to early-stage startups: "Just because customer churn is simple doesn't mean it's not useful. It's probably the only measurement a startup needs to address retention in its infancy."

For larger, established SaaS companies the Subscriber Churn Rate ties into customer satisfaction and helps you determine other important metrics. Dividing 1 by the Subscriber Churn Rate can help you calculate the average customer lifetime: 1 / 0.05 = 20 months.

While Subscriber Churn Rate is a good operational metric, MRR Churn Rate is a vital financial metric.

Monthly Recurring Revenue (MRR) Churn Rate

This is the rate at which MRR is lost from canceled subscriptions of your existing paying customer base (excluding new business).

Calculation: Churn MRR / Start of Period MRR

In comparison with the Subscriber Churn Rate, the MRR Churn Rate is a financial metric which shows the impact of churn on revenue for your SaaS company.

The MRR Churn Rate also helps you identify which customer cohorts are churning.

Through his work with SaaS companies, Tomasz Tunguz has observed SMB's churn at a much higher rate than larger and enterprise business customers. He created the table below to illustrate his observations on churn rate by customer segment:

"SMB customers tend to go out of business more frequently than bigger businesses. They switch products more regularly because switching costs are low," explains Tunguz.

For your own SaaS, you'll also want to analyze MRR Churn Rate to see if lower MRR customers are churning or if you're losing high MRR customers, which will have a bigger impact on your revenue.

MRR Churn Rate "can also help you understand if those losses are manageable, especially when you compare it to the MRR associated with new customers you are bringing on each period. As you move forward and your business begins to grow, it can even help you forecast future revenue performance," writes Sandhya Nakhasi, former Portfolio Operations Manager at Lighter Capital.

It is important to track MRR Churn Rate early on in your SaaS company's lifecycle. It may be tempting to focus on new MRR growth in the beginning but MRR can be steadily growing at the same time MRR Churn Rate is high (or increasing).

Think of MRR Churn Rate "as a sort of early-warning system for your SaaS business. By tracking your MRR Churn early on, you can identify problems that may not show up right away if you're just tracking MRR, giving you time to pivot before your company goes bust," advises Nakhasi.

> "If you charge per user or have different pricing tiers, revenue churn lets you put a dollar amount on what churn is actually costing you, and at what velocity. Revenue churn can be drastically different than customer churn, and will often tell a completely different story."
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> 
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> **Steli Efti,**
> CEO of Close.io

Segment	Monthly Customer Churn %	Annual Customer Churn %
SMB	3-7%	21%-58%
Mid-Market	1-2%	11%-22%
Enterprise	0.5-1%	6%-10%

Gross MRR Churn

Gross MRR Churn is the sum of MRR lost from both canceled subscriptions and downgrades (contraction).

Calculation: Churn MRR + Contraction MRR

Similarly, the Gross MRR Churn Rate is the rate at which MRR is lost from both canceled subscriptions and contraction.

Calculation: (Churn MRR + Contraction MRR) / Start of Period MRR

Some SaaS industry experts consider these metrics a more "honest" look at the health of the business because Gross MRR Churn metrics don't "sugarcoat" the numbers by including expansion MRR (which is included in Net MRR Churn, below).

Low Gross MRR Churn helps indicate a healthy business and it is one of the metrics potential investors pay attention to.

"The quickest way to build your SaaS company valuation is to keep current customers paying for 50+ months (means 2% or less gross monthly churn) and drive expansion revenue from current customer base (negative net monthly churn)," advises Nathan Latka, CEO of The Top Inbox.

How do you determine the acceptable Gross MRR Churn for your own SaaS company? While Bruehl advised the metric should remain below 2%, Lincoln Murphy emphasizes your own metric should be as low as possible. He gives the following example: your Gross MRR Churn Rate is too high if you ended the year with a lot of new subscribers but approximately the same amount of revenue.

"Lots of churn definitions out there. It all boils down to a low Gross MRR Churn indicates if a business is healthy. Net MRR can be 'improved' by expansion, but if the Gross MRR Churn is above 1-2% there seems to be an issue with the product or the ROI story."

Alexander Bruehl,
Founder of SaaS Garage

Net MRR Churn

Net MRR Churn is the sum of MRR lost from canceled subscriptions and contraction plus MRR gained from expansion (upgrades) and reactivation (cancelled accounts that come back).

Calculation: (Churn MRR + Contraction MRR) + (Expansion MRR + Reactivation MRR).

Another important metric is Net MRR Churn Rate, which is the rate at which MRR is lost (or gained) from canceled subscriptions and contraction plus MRR gained from expansion and reactivation.

Calculation: Net MRR Churn / Start of Period MRR

"Not only does net churn more accurately portray your revenue churn, but it's important to your company's overall strategy," says Efti.

Net MRR Churn metrics combine both unhappy (churn/contraction) and happy subscribers (expansion/reactivation). These metrics give you the full picture so you can see how you're succeeding and failing.

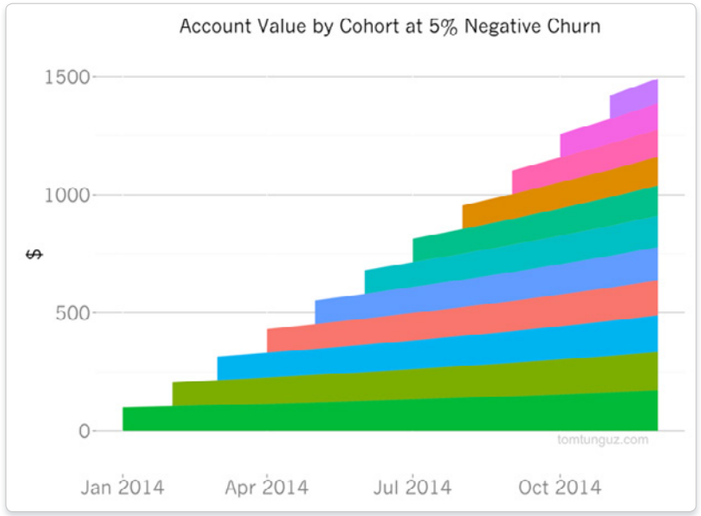
Because Net MRR Churn metrics include "cross-sells, up-sells, organic growth within a customer account, and price increases" they're important as broader metrics "which tell the story of what would happen to a SaaS business over time if it did not acquire any new customers," according to Todd Gardner, founder of SaaS Capital.

Negative Churn

It is important to note Net MRR Churn Rate is the only churn rate metric that can be negative because it is calculated using Net MRR Churn.

"Negative churn indicates the value of your existing customer base is growing without factoring in any new business," explains our own Adam Feber, Marketing Director at Chargify.

Tunguz has a great post on negative churn (definitely worth the read), and he gives the following example of a company which has achieved 5% negative churn:



> "The holy grail in a SaaS business is reaching net negative revenue churn. Negative monthly revenue churn signals a SaaS company that has mastered making customers happy and ultimately selling them on new products and services."

Nathan Latka
CEO of The Top Inbox

The company may lose "5% of its customer base each month, but the remaining 95% of the customers grow their spend with the startup by 10 percentage points, so the total revenue from the cohort is equal to 105% of the revenue from the previous month. Like a savings account, each month, every cohort becomes more valuable."

Even if you've achieved negative churn or a low net churn, there is always room for improvement "because gross churn can be a more accurate measurement of how your SaaS tool and customer success team is working," reminds Jesse Pärnänen, Business Development & Partnerships Manager at Leadfeeder

Breaking Out Voluntary vs. Involuntary Churn Calculations

Chargify's subscription analytics suite automates all the churn calculations above, which typically factor in both voluntary and involuntary churn. However, as we are covering in this eBook, not all churn is created equal.

In addition to the aforementioned churn metrics, Chargify provides detailed Revenue Retention metrics that isolate out involuntary subscriber and revenue churn.

	Entered Dunning	0-3 Days	4-7 Days	Recovered 8-14 Days	15-21 Days	> 21 Days	Still at Risk	Lost
Jul 2016	$528 22	$168 7	$120 5	$0.00 0	$0.00 0	$0.00 0	$0.00 0	$240 10
Aug 2016	$744 31	$240 10	$144 6	$24 1	$0.00 0	$0.00 0	$0.00 0	$336 14
Sep 2016	$816 34	$264 11	$240 10	$48 2	$0.00 0	$0.00 0	$0.00 0	$264 11
Oct 2016	$696 29	$336 14	$96 4	$24 1	$0.00 0	$0.00 0	$0.00 0	$240 10
Nov 2016	$600 25	$144 6	$240 10	$24 1	$0.00 0	$0.00 0	$0.00 0	$192 8
Dec 2016	$864 36	$336 14	$120 5	$48 2	$0.00 0	$0.00 0	$0.00 0	$360 15
Jan 2017	$912 38	$168 7	$192 8	$72 3	$0.00 0	$0.00 0	$0.00 0	$480 20
Feb 2017	$264 11	$72 3	$24 1	$0.00 0	$0.00 0	$0.00 0	$120 5	$48 2

This level of granularity allows to break out churn to understand how voluntary and involuntary churn impact top-line churn metrics. For example, if combating revenue churn is going to be a company priority, you'll need to understand what percentage of revenue churn is voluntary vs. involuntary to define your strategy, set benchmarks, and accurately measure movements.

Actionable Ways To Combat Voluntary Churn

As you have probably gathered, voluntary churn isn't as clear cut of involuntary churn. Because of this, there are many different underlying problems that result in voluntary churn. Below we will cover some of the common problems and actionable solutions you can implement to combat these problems.

There are two primary buckets that lead to voluntary churn:

1. **Desired Outcome Churn** happens when your customers fail to hit their goals (known as their Desired Outcome) with your product. When we talk about voluntary churn, this typically one of the primary causes, and most importantly, it's something you can directly influence and improve.
2. **Natural Cause Churn** is a by-product of the unavoidable problems that sometimes crop up with the SaaS business model. These problems can't always be avoided, but it is possible to take steps to severely limit the harm they cause to your customers.

But first, an important Public Service Announcement! Every business is different which is why it is so important to dig deep into the underlying causes of voluntary churn. Creating feedback loops and exit surveys will help identify which areas contain the biggest red flags and/or where small, quick improvements can make a big impact.

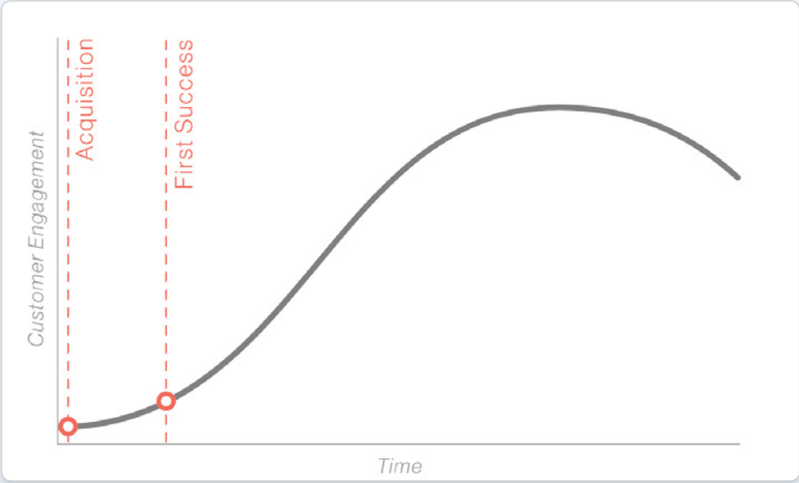
Desired Outcome Churn: Bad Onboarding

The majority of your customer churn is going to take place between two pivotal milestones:

1. Your customer signing-up for your product
2. Your customer achieving their first "success" with your product

People pay for a SaaS product because they want it to solve a problem for them, whether that's speeding up their invoicing or generating more leads. If you're too slow in helping them reach their first success, you're going to see churn, as they look for more immediate ways to reach their goals.

Solution: A great onboarding process bridges the gap between those two milestones, allowing you to lay a defined path for your customers to follow from sign-up to first success. So, to reduce churn, identify the first success your customers are aiming for, and create an in-app tutorial or email sequence to help them achieve it.



Groove's graphic above does a great job of illustrating the "gap" between acquisition and first success. Miss that first milestone, and your customer is out of there.

Desired Outcome Churn: Lack Of Customer Success

Even if you're able to help your customers achieve early success with your product, there's no guarantee they'll continue that success days, weeks, and months down the line.

Your customers' Desired Outcomes are usually big, multi-stage goals, like "increase profitability" or "free up time." To achieve those outcomes, they need to make continual progress towards a series of smaller goals, like "send invoices faster" or "allocate 3 processes to a team member." If those small successes quickly dry-up, churn becomes a real risk factor.

Solution: Helping customers make continual progress is literally the definition of Customer Success. By trying to understand their goals, and doing everything you can to help them move closer and closer towards their Desired Outcome, you can take a proactive stance in the battle against customer churn.

Desired Outcome Churn: Bad Support

All-manner of problems can crop up during the day-to-day use of your SaaS product, from mislaid invoices to confusion over in-app settings. To prevent these problems from becoming deal-breakers, and driving your customers away from your service, you need to offer fast, responsive customer support. If your fraught customer has to battle through dozens of phone menus to speak to a disinterested support rep, their chances of churning are likely to increase.

Solution: Thankfully, the fix is relatively simple: make customer support a priority, and be there when customers need you, using live chat tools and dedicated Customer Support staff.

Desired Outcome Churn: Competitor-Driven

Even if you're able to help customers achieve their desired outcomes, they'll still churn if they believe a competitor will do a better job.

Solution: The quicker you can help customers reach that first success milestone, the lower the chances of this happening. You can also combat this with specialisation: if you're able to differentiate yourself from other SaaS solutions (in terms of your unique expertise, product features or customer service), it becomes much harder to directly compare you to a rival.

Desired Outcome Churn: You Closed The Wrong Deal

Sometimes there's a disconnect between what a customer believes your product can do, and what it can actually do. This is the ultimate example of desired outcome churn: your SaaS product will never help your customer hit their goals because, well, it's the wrong product for the job.

This is most commonly caused by attracting the wrong type of people to your product, either through a lack of understanding of what your ideal customers look like, or through unclear messaging and product information.

Solution: The best way to avoid this type of churn is to understand your ideal buyer persona in as much depth as possible. By using surveys and interviews to hone in on their needs, you can turn your website into the ultimate self-selection tool: broadcasting a clear, defined message, designed to appeal exclusively to your buyer personas.

Natural Cause Churn: Cash Flow Crisis

If you sell to businesses, at some point you'll run into a customer suffering from a cash flow problem. Whether it's a temporary or a longer-term issue, if your product and/or service isn't viewed as a priority, there's a chance your contract will find itself on the chopping block.

Solution: The best way to avoid this is to move your SaaS business higher-up their list of priorities, and ensure that you're viewed as an essential service, instead of just an extra cost. Everything we've said about generating immediate value will help here, but you can also look to increase your contract length (it's easier to ditch a 1-month rolling contract than it is a 6 or 12-month commitment) and move to an automated recurring payment solution.

Natural Cause Churn: Loss Of Key Users

Software adoption is often led by a handful of key people. These product evangelists are your biggest allies. If they leave the company, the fate of your SaaS solution is left in the hands of less interested parties, which creates a serious churn risk.

Solution: The best way to combat this is to get your SaaS into the hands of as many team members as possible. Freemium companies like Slack and Evernote have mastered this approach, but you can achieve similar effects with a paid model by incentivising user referrals, and making them a core part of your onboarding process.

Natural Cause Churn: Product Problems

Down-time is an almost inevitable part of running a SaaS business, and if your service outage has a real impact on a couple of customers, there's potential for churn.

Solution: Tackle this by responding to the issue quickly and clearly, acknowledging the problem, and outlining your steps for solving it. If you've had a serious problem, it can sometimes be worth offering short-term discounts to the customers affected: taking a temporary hit to cashflow is usually much better than losing a customer for good.

Natural Cause Churn: No Chemistry

A lot of SaaS businesses take a pretty hands-on approach to their service: whether that's personally onboarding early-stage customers (the concierge MVP approach), or offering consultation services to work alongside the product.

But whenever people are involved, there's also the possibility of personality clash. The more time customers spend in contact with your team, the greater this problem can become, even contributing to churn.

Solution: To help avoid this, you can be more proactive in pairing customer service reps and consultants with right-fit customers, and by having a process in place for quickly switching customers to different reps.

Natural Cause Churn: Leaving The Early Market

Early-stage SaaS companies attract very different types of people to more polished, refined solutions.

If you're in open beta, you'll attract early adopters: the tech enthusiasts that enjoy playing with buggy, unfinished products, and want to contribute to its development. But as product development continues, and you edge ever closer towards a finished product, there'll be less opportunities for these early customers to engage.

Solution: The more refined you become, the more mid-market customers you'll attract, looking for a fully-functional, proven solution. As you start to engage this new market, you'll slowly lose your original audience to churn. This shouldn't be viewed as a problem: making the transition into bigger markets is a necessary part of growth, and mid-market customers have far deeper pockets than early adopters.

Use Voluntary Churn To Iterate & Improve

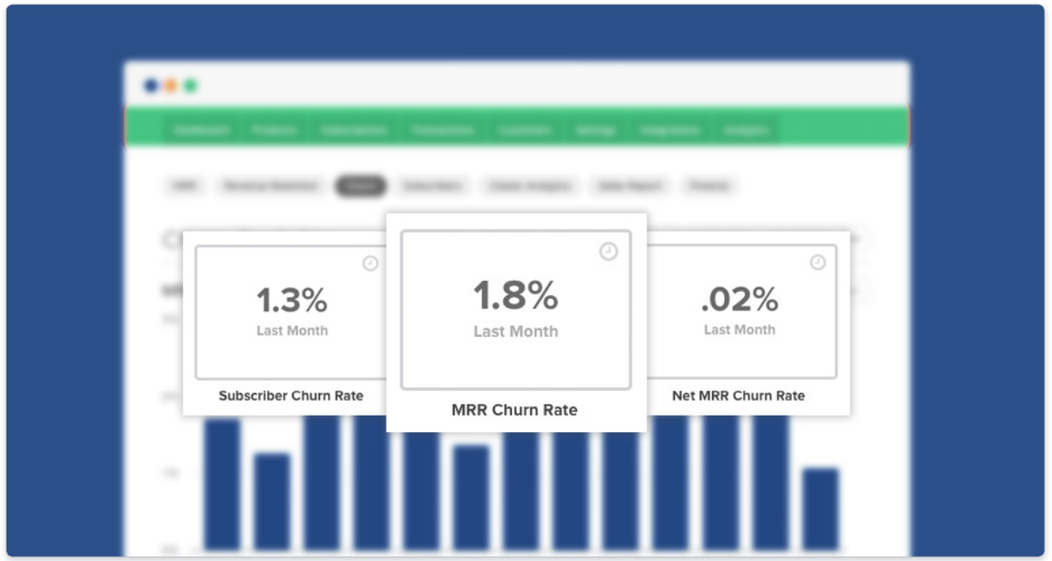
One unique trait of voluntary SaaS churn is that there is typically a gap of time between when a customer cancels and when their subscription actually runs out.

This gap is an opportunity to attempt to win back the customer, or at a minimum, gather feedback on why they canceled to help combat future occurrences.

We should note that some customers are better to let go without a fight. A few examples of customers you wouldn't want to win back:

- The one that subscribed without understanding that your product wouldn't really solve their problem—that relationship was doomed from the beginning
- The customer that has complex needs that your product/service does not meet and does not plan on meeting. These customers can be a pain, requesting features you can't offer and eating up your support team's time.

In these cases, it's best for the both of you to admit your product wasn't the right solution and cut bait. Freeing up this time will allow your team to focus on canceled customers who have a problem you can resolve.



Communication Is Key!

If you don't have an exit survey that is presented to and/or goes out to all customers that cancel, this is your first step! The information you can glean from this survey is worth its weight in gold—not only should it tell you about gaps in your product, it should also provide enough insight to attempt to win that customer back.

For instance, you might receive a response like "I needed the product to do x but your product would only give me y." Having such a clear description of what the customer needs could enlighten your team, informing them about a feature already in place, which may or may not solve the customer's problem.

More often than not, it isn't that clear, and you'll need to reach out to the customer for further information. At this point, you should be calling (not emailing) your canceled subscriber.

"Get your churned customer on the phone. Only do email as a last resort. Having a real conversation with your departing customer is integral to learning something meaningful from the exercise. It's all about going deeper, asking questions, and coming to a real, detailed understanding of your customer," says Steli Efti, CEO of Close.io.

After you've identified the issue that led to the cancellation, you're ready to move on to the next step.

Attempt To Align Solutions With Each Customer's Problem(s)

If you discover that your canceled subscriber's issue has to do with pricing, then the solution you offer should tie back into pricing.

Here are some pricing strategies that may help you retain those customers with a foot out the door:

- **Upgrade.** If the customer canceled because their business has scaled and it seemed your product wasn't able to scale with them, an upgrade to a higher tier may provide them with the additional features or support they need.
- **Downgrade.** Conversely, downgrading to a lower tier can help you fit a customer's budget while still allowing them to use your product. If a downgrade entails a loss of features or support, make sure these elements aren't vital to the customer's success with your service.
- **Share upcoming feature releases.** By offering churning customers a glimpse of what's coming down the line, you can excite them about future releases. Things that inspire people to stick around are usually features, which save time (e.g., better importing), increase efficiency (e.g., integrating with third parties), or offer additional value for no extra work (e.g., weekly reports)." Be sure to share only feature releases that are guaranteed to come out soon— otherwise you risk the ire of a customer who agrees to stay on but has to wait around for a needed feature.
- "**Offer partner services** to help them bridge success gaps," suggests Lincoln Murphy, growth architect at Sixteen Ventures. Murphy advises always giving a customer at least one partner integration option that would allow them to continue using your product rather than canceling outright.
- **Allow for short pauses** in accounts. If your subscriber's business is seasonal, having the ability to pause their account during the slow season will mean that they're already plugged in when that busy time arrives.
- **A pricing discount.** We don't recommend this strategy be used often because discounts can weaken your brand perception, but it does have a time and place to win back a customer—read more on our blog "Should Discounting Be Part of Your SaaS Pricing Strategy?"

Consider, too, whether all your tiers and pricing options are clear to current and prospective customers. You may be able to head off some cancellations at the pass with good recurring billing platform that can handle the options you'd like to offer. Chargify can help you there.

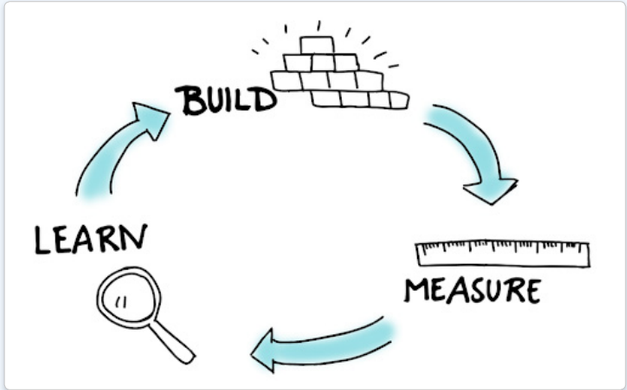
Thanks to technology, "particularly more-sophisticated customer databases, companies…draw on information about how people used their service the first time around to craft more-successful win-back offers and to identify and go after the most profitable defectors," according to Harvard Business Review.

Finally, it is essential to weigh the opportunity costs of the resources it takes to win back canceled customers before they churn. "Knowing what kinds of offers lure back the most customers isn't enough; the costs and returns of each are important too," reminds HBR.

Don't Let Voluntary Churn Go To Waste!

In an ideal world, you would retain every customer you talk to, but let's be realistic: that isn't going to happen.

Don't let those conversations and feedback from canceled customers go to waste. This feedback loop is massively important—you can use what you learn from canceled customers as a way to improve your offerings.



Depending on the issues you're learning about thanks to those cancellation conversations, you may want to look at:

- Improving communication
- Improving customer support
- Improving onboarding
- Adjusting pricing
- Offering trials—or not; other considerations include trial length and whether to request a credit card prior to trial signup
- Investing in marketing to refresh your value proposition
- Reviewing buyer personas and how you're currently marketing to those personas
- Ensuring your sales teams are setting proper expectations

Now that we've covered plenty of information about underlying causes of voluntary churn and how to combat it, let's dig into the world of involuntary churn. Spoiler alert, it has very different causes and solutions…

Actionable Ways To Combat Involuntary Churn

With their global reach and popularity, particularly for transactional e-commerce, it's easy to see why credit and debit cards have become the default payment method for subscriptions businesses. But cards weren't designed for recurring payments. They operate on a complex infrastructure with multiple players, creating plenty of opportunity for failure which is the primary cause of involuntary churn.

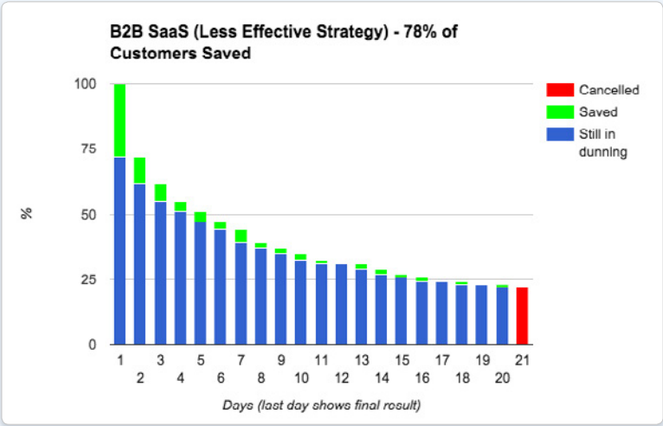
This is because over time, stored card details become outdated as cards expire (typically every three years), or are cancelled, after being lost or stolen. They can also fail because a customer hits their spending limit.

While there are many ways to mitigate involuntary churn risks caused by cards, there are also other alternatives payment methods specifically designed to reduce involuntary churn. In this section, we will shed light on your involuntary churn prevention options.

A Dunning Strategy For Cards Is Mission Critical

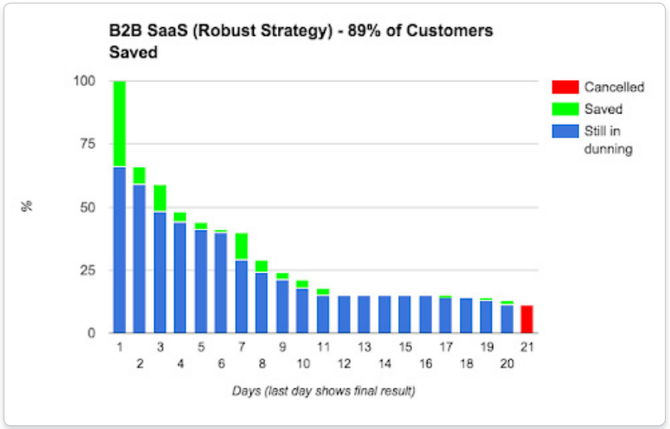
Dunning is the process of communicating with customers to collect payment of past due accounts—caused by failed transactions—prior to account cancellation. With failure rates for credit cards ranging between 10 - 25%, it is extremely important that you have a dunning strategy in place.

Chargify offers a suite of tools that allow subscription businesses to customize and optimize dunning communication and workflows for maximum revenue retention. Some of these tools include proactive card expiration emails, customizable retry schedules, and automated reminder emails designed to get updated card information prior to cancelations.



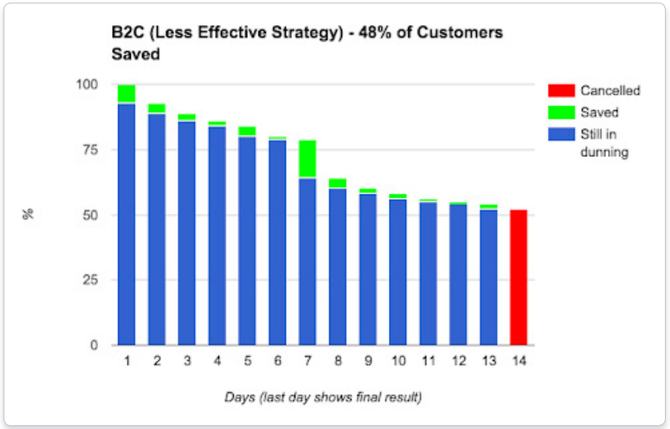
← **Here is an example of a B2B SaaS company prior to the implementation of a more effective dunning strategy using the tools provided by Chargify.**

The same company adopted a more robust dunning strategy, including card expiration emails, renewal notifications and more frequent customized past due notices. They added a link for support issues to ensure that their customers understand that help was available, and they also clearly communicated a cancellation date so that their customers knew the time frame in which they needed to act.

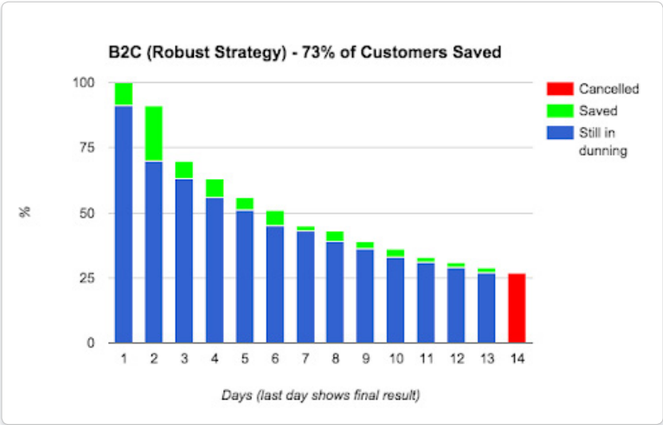


← **You can see that the percentage of recovered revenue increased from 78% to 89%. Over time, these improvements have a big impact on a merchant's bottom-line.**

In the case of B2C, higher churn is often expected but effective dunning can make a dramatic difference. The dunning period is often shorter so a more aggressive strategy may be adopted.



← **A sample B2C company with a minimal dunning strategy yielded the following results.**



← **The merchant used similar tools to the ones described above and also included promotional materials and discounts to achieve a remarkable improvement with 73% vs. 48% of past due customers saved.**

Everyone's results will vary, but we see time and time again that these dunning tactics really work well.

Reducing Involuntary Churn With Account Updaters

Account updater services are a proactive way to reduce involuntary churn - Visa and Mastercard will batch check your customers card details with issuing banks, before each renewal (and you pay a few pence for every set of updated details).

Most businesses access account updaters via an acquirer like Adyen, Braintree and WorldPay (acquirers may build their own logic on top of basic account updaters, for example allowing you to run reports), and/or through their billing software provider.

Card updater services (often paid for by the merchant) will catch a proportion of your failed payments, but their success is dependent on every actor in the complex card value chain doing what it's supposed to. Account updaters may fail for the following reasons:

- A local issuing banks' processor is not opted into or integrated with the scheme (particularly a problem outside the US and Canada, where scheme coverage can be patchy)
- A bank has not yet integrated with the scheme (this can happen even in the US where it's mandatory for issuing banks to participate in these schemes)
- A card is unsupported, e.g. it's international or prepaid
- The card belongs to a card network which doesn't support account updater
- A bank fails to promptly update Visa and Mastercard about a change in card details (since many smaller banks still rely on manual processes)
- A customer switches card provider

Highly Consider Using Direct Debit Whenever Possible

Direct Debit is a bank-to-bank payment method, where the customer pre-authorises the merchant to collect payments directly from their bank account.

As we mentioned above, failure rates for credit cards can range anywhere from 10 - 25% a month. Customers who use Direct Direct through GoCardless have an average failure rate of 2%, with some merchants as low as 0.5%. The primary reason for this is because unlike cards, bank accounts do not expire, cannot be physically lost and are unlikely to be stolen.

So, as a result, Direct Debit helps to significantly lower involuntary churn.

Consider this:

- A business that collects recurring card payments from its customers and has a monthly churn rate of ~6%.
- 30% of that total churn will be involuntary - that is, the result of administrative failure of card payments. So this business is needlessly losing 1.8% of its customers every month.
- Using Direct Debit improves payment success rate, reducing failures from around 10% to around 2%.
- Even with a conservative estimate, this would allow a typical subscription business to reduce involuntary churn from 1.8% to 0.36% - and overall churn from ~6% to ~4.5%.

"Subscriptions are in essence relationships that constantly change over time. In recent years, the ability to offer a menu of payment options has increased in importance for both getting new customers in the door and retaining them as the customer/merchant relationship evolves.

In the US, automated card payments have been the de facto standard for many years, but we've seen an upward trend in revenue processed through ACH payments which increased 112% from 2017 to 2018.

This trend, combined with clear demand signals for Direct Debit payment options from countries like the UK and Australia point to a larger shift in customer preferences when it comes to how automated payments are processed."

Tom Rotem
Chief Executive Officer, Chargify

Alternatives to card payments, such as Direct Debit, may not always be the preferred option for every end-user, it is a very popular option that is on the rise across Europe and the rest of the world. Providers like GoCardless are joining the dots to create a global bank to bank payments network that can support global subscription businesses.

- In 2016, Bank Debit made up 20% of all 122 billion cashless payments taking place in the EU (source: European Central Bank, Payment Statistics for 2016).
- In the UK in 2017, 75% of all recurring payments were processed via Bank Debit (Finance UK)
- More than 50% of non-cash transactions in Germany are processed via SEPA Bank Debit
- 60% of online transactions in the Netherlands are made with bank transfer system iDEAL.

Direct Debit could be exactly what SaaS businesses need. It solves the involuntary churn problem and boosts profit margins in the process. Designed specifically to handle recurring payments, Direct Debit is ideal because bank accounts never expire and can't be physically lost or stolen. And Direct Debit's low failure rates are almost always due to the simple reason of customers having insufficient funds.

Chargify's integration with GoCardless enhances Direct Debit, providing a payment solution specifically designed for companies with subscription offerings. In addition, GoCardless is perfect for US SaaS firms with customers in the UK and Europe because of the range of supported Direct Debit schemes that are available.

This one-stop payments access point also handles all the complex compliance and regulatory issues for you, providing an easy way to start taking European payments, while also enabling your SaaS business to eliminate involuntary churn and increase LTV.

GoCardless and Chargify support payments in the UK (Bacs), across the Eurozone (SEPA), Sweden (Autogiro), New Zealand (Becs NZ), Australia (Becs), Canada (PAD), and Denmark (Betalingsservice) with the US (ACH) coming soon.

Tackling the root of card declines could bring down your failure rate to a low as 0.5%, cutting involuntary churn by more than 70% and bringing down overall churn by 1-3% - ultimately enabling you to increase lifetime value and ROI by more than 30%.

Real-Life Tips & Tricks From Successful SaaS Leaders

As you have hopefully gathered by the information above, reducing churn is mission critical for all SaaS businesses. We write about it, read about it, discuss it, test for it, and even when we've reduced it, we look for ways to reduce it further. While there are many resources on how to reduce churn (including this one), we thought it would be great to have a compilation of tips from successful SaaS leaders.

So we asked SaaS experts and leaders, "What is that one tip for reducing SaaS churn that you wish someone had told you when you first started?" Below are the answers we received.

"Happy customers are your best way to not only increase TLV (by reducing churn) but also reducing CAC (by increasing word of mouth). Yes, I know this is ridiculously obvious, but I feel like sometimes the obvious gets lost in the maze of metrics."

Brian Halligan
Co-Founder & CEO, HubSpot

"I'd say the best way to reduce churn is always to improve the product. That's #1. Second to that, many companies — especially those with sales teams — can make a lot of progress by better aligning their pricing, packaging and sales rep compensation to match their customer retention goals. Examples include things like moving from monthly to annual contracts; providing or requiring services to help companies get setup properly; and holding the sales team accountable for retention of the deals they bring in. All the stuff that can have a big impact in the short term while the company grinds away at creating a remarkable product."

Brad Coffey
Chief Strategy Officer, HubSpot

"Even though it is only one piece of a customer's lifetime, focus the majority of your time on the first 30 days and activation. Activation is not getting signed up and paying, but that the customer has taken an action or set of actions that indicate they understand the meaningful value that your product provides. Improvements on activation have the largest effect on overall churn for many reasons. The primary reason being that once a customer/user forms an opinion about a product/service it becomes much harder to change that opinion after the fact. So if they don't have a good activation experience you will have to work multiple times harder to retain them over the long term compared to if they had a good activation experience."

Brian Balfour
Founder & CEO, Reforge

"The most powerful thing you can do to reduce churn is going to sound simple and obvious, but so few actually take the time to do it: build a real relationship with your customers. Find out who they are, what they want, what they don't want, and how you can make them happier than they could ever be with your competitors. Every customer that signs up for Groove gets an email from me with a personal welcome and a simple question: why did you sign up for Groove? I read every response, and we get huge insights from this about each customer and what success actually means to them, which helps us create a better experience that's tailored to their needs.This is email is just one of the things we do to accomplish this, but if there's one thing I wish I had done more of when we were just starting out, it's getting to know our customers and building deep relationships."

Alex Turnball
Founder & CEO, Groove

"I wish someone had told me how important it is to view churn as a learning opportunity. We now try to do exit interviews with every customer who churns and the feedback is authentic and timely.In these conversations, we've discovered major opportunities for improvement in our product. We've learned more about their desired outcomes, and what we'd need to change to help them reach it. The insight we get informs our strategy and how we prioritize our product roadmap. It allows us to solve for the root cause of churn and hopefully prevent it before it happens for future customers. We also don't stop at exit interviews. Just because someone stops paying you doesn't mean they stop rooting for you. We like to think of churned customers more like alumni than strangers. If they're still willing to talk to you and provide feedback, they can be hugely valuable. And who knows, maybe you could win them back one day."

Jackson Noel
Co-Founder, Appcues

"Great on-boarding is the best place to ensure that you don't have customer churn. The insight here is obvious: right after purchase the customer is most excited about the product. They will give you time to get things working. If you don't meet their expectations at that time it is much harder to fix things later, as they have moved on emotionally. So building a great on-boarding program is step one, and then step two is to ensure that your on-boarding was successful using a survey at the end. Ideally this should provide you with a measurement that you can use to identify problems and resolve them early."

David Skok
General Partner, Matrix Partners

"In my experience, the most effective thing you can do to reduce churn is to on-board your customers properly in the first place. It's maybe obvious, but you can only be successful if your customers are successfully using your product."

Christoph Janz
Co-Founder & Managing Partner, Point Nine

"SaaS subscriptions are not like gym memberships! Early in the year, I see lots of people commit to a gym membership with all the best intentions. But after 3 or 4 months, many of them are concocting all kinds of clever excuses for not actually going. But here's the thing... they keep paying the monthly fee. Maybe it's guilt or they're expecting a sudden jolt of motivation. Subscriptions for SaaS solutions don't usually work that way. Unlike the gym membership, if a few months go by without the customer using the SaaS solution, they will stop paying for it. Companies need to get their customers on board, keep them engaged, and show them value week in, week out. It's a lot of work, and customers won't do it all on their own. Companies need to keep marketing, even to their existing customers."

Peter Cohen
Managing Partner, SaaS Marketing Strategy Advisors, Inc.

"I recommend building a robust Client Success function into the business on day one. Many SaaS founders view this as a 3rd or 4th step – after they have nailed product, marketing and sales, but the reality is that building a dedicated client success function from the start can have a huge impact on retention. I feel so strongly about this that, in our most recent company (which is still in stealth mode), our very first hire was a Customer Success Manager."

Kristian Andersen
Partner, High Alpha

"Design all of your metrics and incentives to promote customer retention — including sales and marketing. It's easy to game your metrics, and people are driven by incentives. If you want to reduce churn, start by making sure every team and department is customer-driven and aligned around customer success. As Charlie Munger said, the most important rule in management is to get the incentives right."

David Cancel
CEO, Drift

Want To Learn More

Both Chargify and GoCardless are changing the way subscription businesses operate by providing the tools and resources needed to stand out in a sea of SaaS. Visit chargify.com and gocardless.com to learn more about each company.